United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

ORIGINAL 75-7327

To be argued by
EDWARD L. SADOWSKY

United States Court of Appeals
SECOND CIRCUIT

DORSEY & CO., INC.,

Plaintiff-Appellant,

against

BANQUE NATIONAL DE LA REPUBLIC D'HAITI,

Defendant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT—
SOUTHERN DISTRICT OF NEW YORK

APPELLANT'S BRIEF

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Issue Presented for Review

Did the appellant have a duty to mitigate damages prior to learning of the wrong done to it by the appellee?

Statement of the Case

This action arises out of the negligence of the appellee (hereinafter "Banque") in handling stock certificates and drafts totaling $628,434.64 transmitted to it for collection by The Hibernia National Bank (hereinafter "Hibernia Bank"), the agent of appellant (hereinafter "Dorsey"). Dorsey is a stock brokerage house located in New Orleans, Louisiana, and obtained a judgment for damages it sustained as a result of the Banque's mishandling of the stocks purchased by Dorsey for the account of two of its customers, Robert Tomarkin, purchasing as Williams In-

vestors, and Lloyd Whitkind, purchasing as Whitkind Realty (hereinafter "Tomarkin" and "Whitkind") (3a-15a; 18a; 65a).*

Following a trial without a jury in the United States District Court for the Southern District of New York, District Judge Edward Weinfeld, applying the law of Haiti to the issue of the liability of the Banque to Dorsey, found that the Banque was negligent, and that negligence was the proximate cause of the losses Dorsey seeks to recover (7a-8a; 11a-13a). The court further found that Dorsey was in no way contributorily negligent in the transaction (9a-13a). He awarded damages to Dorsey in the sum of $35,687.50 with interest from October 2, 1972 (18a).

The court found that the Banque had been instructed, via collection letters accompanying the stock certificates and drafts, to deliver them against payment by Paul Supart & Co. (hereinafter "Supart & Co."), the drawee, and to remit the proceeds by cable. The Banque was further instructed that in the event of non-payment of the drafts, delay in payment or acceptance, or dishonor, it was to notify Dorsey's agent, the Hibernia Bank, promptly, stating the reasons therefor (3a-4a).

Although all documents were received by the Banque on or about September 29, 1972, the drafts were never presented, payment was never received, the Hibernia Bank was not notified promptly of delay in payment or acceptance nor of the non-existence of Supart & Co. The Hibernia Bank received the certificates and drafts, which arrived by steamship on December 22, 1972, "by which time the value of the shares was considerably lower than on the date when the Banque received them on September 29, 1972" (4a-5a). Dorsey was then unable to collect payment from its customers and sold the securities at a loss in May 1973 (4a).

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* Numbers refer to pages in the Appendix to the Brief on Appeal.

Although the Hibernia Bank cabled, telephoned and communicated by letter with the Banque throughout October and November of 1972, seeking information as to the receipt of the documents and as to whether they were paid, it was not until December 1972 when an investigation was first conducted at the Banque, and it was discovered that a mail clerk had, in error, returned the documents to the post office for return to sender on September 30 (5a-7a). In the opinion of the court, the Banque's negligence consisted of its failure to make a prompt inquiry in reply to the Hibernia Bank's first cable on October 2 "and thereafter when cable after cable was sent" (7a).

As the court stated, "Not only did the Banque fail to follow the instructions in the collection letters, thereby violating its acknowledged practice of following instructions accompanying drafts, but it subsequently compounded its negligent conduct over a two and a half month period by failing to conduct a prompt investigation after the Hibernia Bank's repeated inquiries, and by misleading the Hibernia Bank and the plaintiff into believing that the Banque had not received the drafts and certificates" (11a-12a).

In addition to its negligent handling of the documents, the Banque compounded its injury to Dorsey by failing to advise Dorsey that the latter had been victimized by a fraud and, indeed, by affirmatively misleading Dorsey into believing that no fraud had been committed.

As the trial court found, Dorsey, on behalf of its customers, Whitkind and Tomarkin, had previously presented securities for payment which it had purchased for these customers. On six or seven occasions payment was made by a drawee in Canada, and Dorsey had never experienced any difficulty (11a).

However, in connection with the transaction which is the subject of this action, the Banque testified that Supart & Co. not only did not have an account at the Banque

but one did not exist in Haiti (126a-127a; 131a; 134a-136a). Yet the Banque knew very early after the documents were received that Dorsey was seeking to collect against delivery from Paul Supart & Co. (126a-127a; 134a-136a). On two occasions Dorsey's agent, the Hibernia Bank, in an effort to trace the lost documents, advised the Banque that the account to be charged was Supart & Co. (132a; 134a-136a; 5a). Yet the Banque concededly took no steps to advise Dorsey or the Hibernia Bank that no such account existed (134a-136a). More importantly, when the Banque finally admitted its negligence and apologized in its cablegram of December 19, 1972 (19a), it specifically requested that Dorsey return the documents to the Banque for collection, the plain implication being that an account existed in Haiti against which the funds would be collected.

Dorsey, for its part, did not learn that Supart & Co. did not exist until it took the pre-trial deposition of the Banque (76a). Moreover, it never could learn the true state of affairs from its customers Whitkind and Tomarkin because they refused to testify on the grounds of possible self-incrimination, and their right to invoke the privilege was upheld by the District Court (124a).

After December 22, Dorsey took steps to present the items for payment (72a; 110a-121a). Failing to receive payment from its original customers, it finally sold the stock in May 1973, sustaining a loss of $356,021.95 (72a-74a).

The court, however, held that Dorsey was entitled only "to recover damages based upon the difference between the value of the securities on the date the Banque received them plus a reasonable time for presentation for payment to the drawee and notification of non-payment, in this instance, October 2, 1972, and their value upon the date they were received, December 22, 1972, when they could have been sold by plaintiff in the event its customers did not make payment" (14a).

Dorsey appeals from that portion of the court's Findings of Fact and Conclusions of Law that deny it complete recovery of the loss it sustained between October 2, 1972 and when the securities were sold in May 1973 (72a-74a).

ARGUMENT

Dorsey was not required to mitigate its damages by selling the securities immediately on their return.

The decision of the District Court overlooked the fact that the Banque was, in effect, guilty of two torts. If the only wrong committed by the Banque was to have negligently handled the securities by failing to follow properly the Hibernia Bank's instructions and by failing to respond to the cables of inquiry, it might be argued that its liability should be limited to the securities' loss in value during the period in which Dorsey was deprived of them. However, the Banque committed a second tort when it failed to advise Dorsey that Dorsey had been victimized by a fraud and that Supart & Co. did not exist, and particularly when it affirmatively misled Dorsey into believing that the funds were collectible in Haiti. In the light of this second tort, Dorsey had no duty whatsoever to mitigate damages by selling the securities on December 22, 1972, and the damages attributable to the negligence of the Banque should not be so limited.

The second tort began when, on October 20, 1972, the Hibernia Bank, in attempting to trace down the lost securities, cabled the Banque and advised that the drafts were to be collected from Supart & Co. The Banque failed, upon receipt of the cable, to advise Dorsey or the Hibernia Bank that it had no knowledge of that account, despite the claim of the Banque that every employee would be capable of giving such advice (8a; 126a; 134a-136a).

Again, on November 16, 1972 actual copies of the collection letters (5a-6a; 134a-136a) were transmitted to the

Banque, who, upon their receipt, had full knowledge of every detail of the transaction and the account against which the funds were to be collected. It still failed to advise Dorsey or its agent that the account did not exist.

These two acts of omission on the part of the Banque pale when compared with the affirmative deception resulting from its cable of December 19, 1972, wherein the Banque stated that it stood ready to collect the very items in suit, clearly implying that there was an account at the Banque in the name of Supart & Co. and that Supart & Co. stood ready to pay the items against delivery of the stock (19a).

Indeed, Dorsey did not even know until after the commencement of the action that it had been misled by the Banque with respect to the non-existence of Supart & Co. (76a). Clearly, on December 22, 1972, as the court reasoned, the stocks "could have been sold by [Dorsey] in the event its customers did not make payment" (14a). However, as the court held, Dorsey had no reason to doubt the *bona fides* of its own customers (11a). Because of the Banque's misrepresentations Dorsey did not know on that date that its customers would not make payment, and it had no duty to sell.

In effect, the trial judge ruled that Dorsey had a duty to mitigate its damages by selling the stock on December 22, 1972. In *Pearlstein* v. *Scudder & German,* 346 F.Supp. 443 (S.D.N.Y. 1972), the court considered the circumstances giving rise to such a duty. In that case, the plaintiff sued the defendant for losses sustained in the purchase of certain securities which the defendant had illegally sold to the plaintiff. The defendant urged that the plaintiff was obliged to mitigate his damages by selling the securities in a declining market. The court there held that the plaintiff had no such duty:

> "It is axiomatic that in order to have a duty to mitigate damages, one must recognize that he has been

damaged. It would have to appear that he knew or should have known that a tort had been committed against his property, and that he had been damaged as a result of that tort in order to be placed under the duty to mitigate." 346 F. Supp. 452

In reaching that conclusion, the court relied upon *Costello* v. *Costello*, 209 N.Y. 252, 262 (1913), in which the Court of Appeals stated:

> "A wisdom developed after an event, and having it and its consequences as a source, is a standard no man should be judged by."

The *Pearlstein* court found that the plaintiff was not required "to take affirmative action to mitigate his damages" until his knowledge that he had been wronged had "ripen[ed] to a sufficient degree of certainty." He would then be "entitled to a reasonable time thereafter within which to make sales of the securities so as to minimize further loss" 346 F.Supp. 453.

The same common-sense rule should apply here. Dorsey knew, on or about December 20, 1972, that the documents had been returned to the post office in error, but it did not know—and did not learn until after the commencement of the action—that there was no Supart & Co. in Haiti to make payment on behalf of its customers. Thus, Dorsey was under no duty to mitigate damages on December 22, 1972 or at any subsequent time.

In analogous cases under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78; and Rule 10(b)-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, defrauded purchasers of securities have no obligation to sell their stock following discovery of the fraud, but their damages are measured as of the date the fraud was, or should have been, discovered—either by the purchaser or by the public. *Harris* v. *American Investment Co.*, 1975 CCH Fed. Sec.

L.Rep. ¶ 95,208 (8th Cir. 1975); *Beecher* v. *Able*, 1974-1975 CCH Fed.Sec.L.Rep. ¶ 95,016 (S.D.N.Y. 1975); *Cant* v. *Becker & Co., Inc.*, 379 F.Supp. 972, 975 (N.D.Ill. 1974); *Esplin* v. *Hirschi*, 402 F.2d 94, 104 (10th Cir. 1968), *cert. den.* 394 U.S. 928 (1969); see, generally, Note, "The Measure of Damages in Rule 10b-5 Cases Involving Actively Traded Securities," 26 STANFORD L.REV. 371 (1974).

Often, however, as was the case in *Esplin* v. *Hirschi*, *supra*, due to the acts of the defendant, it is not until the discovery of the fraud "that the true value of the securities as an investment can be ascertained. Accordingly, . . . the actual extent of the loss sustained may be ascertained as of the date the purchaser realizes, or should realize, that he had been defrauded." 402 F.2d 104.

The same reasoning should apply herein. Dorsey should not be limited to damages measured as of a date prior to its discovery that it had been misled. It was not contributorily negligent in failing to doubt its customers (11a). And any need to sell which it might have apprehended on December 22, 1972, was obscured by the actions of the Banque.

Furthermore, Dorsey's role was that of agent for its customers, Whitkind and Tomarkin (3a). As such it was under no duty to protect itself in a declining market, but rather had the right to expect full payment from its customers regardless of fluctuations in the market price of the securities.

On December 22, 1972 and in the weeks thereafter, Dorsey sought to be paid in full and had no reason to believe that it had been deceived (72a; 110a-121a). It therefore had no duty to mitigate its damages by selling on that date.

The trial court measured damages by the difference in value of the securities between October 2, 1972 and December 22, 1972 (14a). The proper measure is the difference in value between October 2, 1972 and May 1973 when the securities were sold, or $294,962.31 (3a; 14a; 72a-74a).

CONCLUSION

Dorsey was not required to mitigate its damages by selling the securities immediately on their return, and is entitled to judgment of $2[illegible]4,962.31.

Respectfully submitted,

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MONA D. SHAPIRO

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT--
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AFFIDAVIT
OF SERVICE

STATE OF NEW YORK,
COUNTY OF NEW YORK, ss.:

Nathan Chambers , being duly sworn, deposes and says that he is over the age of 18 years, is not a party to the action, and resides at 510 Atlantic Avenue, Brooklyn, New York
That on September 26, 1975, he served 1 copies of Appendix and two copies of Appellant's Brief;
on

LUNNEY & CROCCO,
Attorneys for Defendant-Appellee,
20 Exchange Place
New York, New York 10005

by delivering to and leaving same with a proper person or persons in charge of the office or offices at the above address or addresses during the usual business hours of said day.

Nathan Chambers

Sworn to before me this
26th day of September , 1975

John V. D'Esposito
JOHN V. D'ESPOSITO
Notary Public, State of New York
No. 30-0932350
Qualified in Nassau County
Commission Expires March 30, 1977